# Investment Management Presentation

## Chandler Asset Management

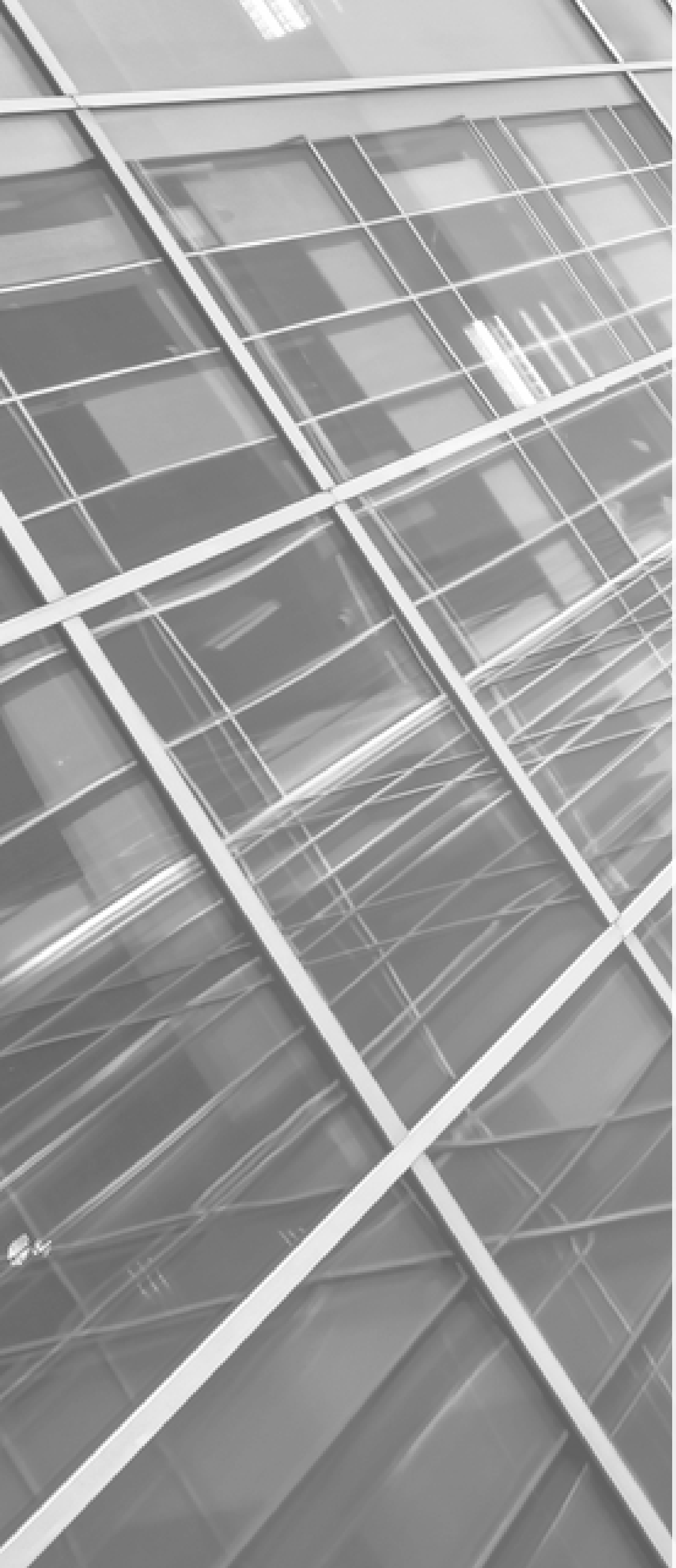
INVESTMENT REPORT

# Orange County Transportation Authority

*Period Ending September 30, 2020*

CHANDLER ASSET MANAGEMENT, INC. | 800.317.4747 | www.chandlerasset.com

# Table of Contents



# Section 1 | Economic Update

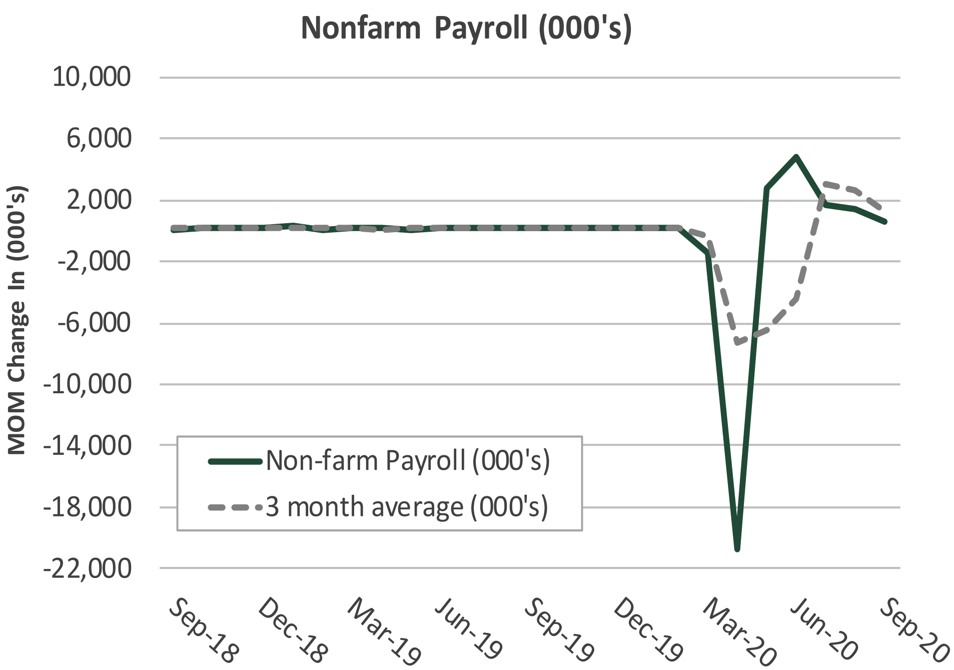
# Economic Update

- The US economy continues to experience a somewhat uneven and slowing pace of economic growth, consistent with more of a U-shaped (rather than V-shaped) recovery, following a sharp decline in economic activity in the second quarter. The outlook for the economy remains uncertain and is largely dependent on the course of the pandemic, the amount of additional fiscal relief, and the timeline for a vaccine, in our view. The Fed's highly accommodative monetary policy framework, along with a swift and robust fiscal policy response from the government earlier this year, has provided support for the financial markets amid a challenging economic backdrop. However, we believe financial markets are poised for increased volatility through year-end due to the upcoming election, a resurgence in virus cases, and an unclear outlook for additional fiscal relief. If the expected timeline for a COVID-19 vaccine was pushed into second half of next year or beyond, we believe that would fuel a significant amount of financial market volatility.

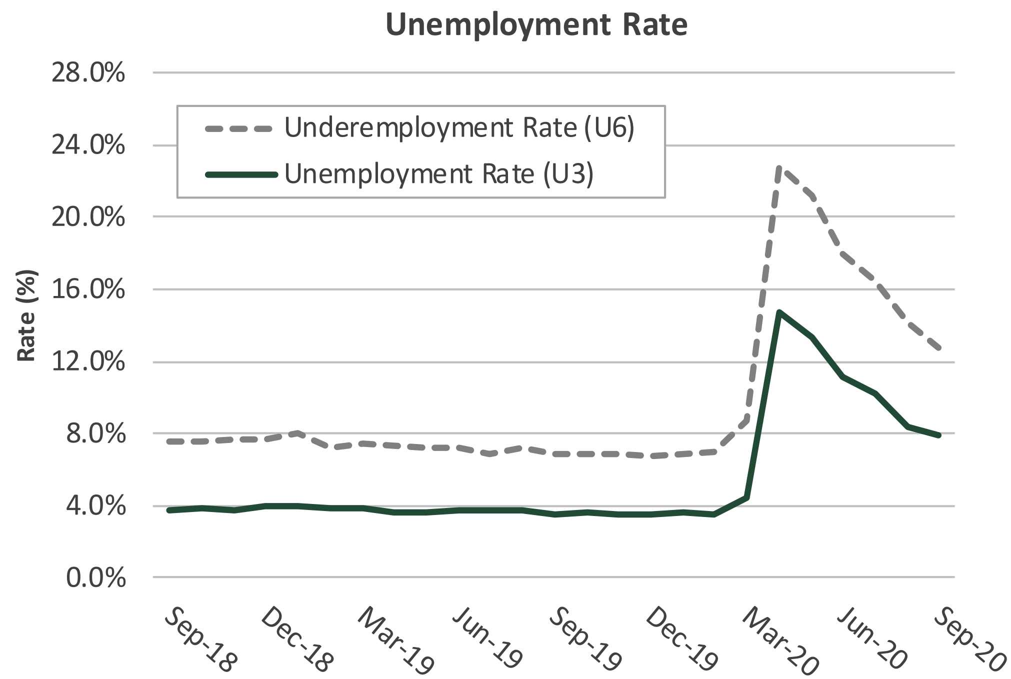
- The Federal Open Market Committee (FOMC) kept monetary policy unchanged in September with the fed funds target rate in a range of 0.0% to 0.25%. Monetary policy remains highly accommodative and Fed Chair Powell maintained a dovish tone during his press conference. The Fed will continue to use its balance sheet to support smooth financial market functioning by purchasing Treasury and agency mortgage-backed securities and will continue to use its lending facilities to support the flow of credit to businesses and municipalities, as needed. In the September policy statement, the FOMC noted that inflation continues to run below its 2.0% target, as weaker demand and lower oil prices are holding down consumer prices. Longer-term, the FOMC will allow inflation to run above 2.0% for some period of time before it looks to tighten policy, which implies the fed funds target rate will remain anchored near zero for years. The Fed's updated summary of economic projections signals that the target fed funds rate will remain unchanged through at least 2023, as policymakers do not expect inflation to exceed 2.0% during that timeframe.

- On a year-to-date basis, the yield on 2-year Treasuries was down 144 basis points to 0.13% and the yield on 10-year Treasuries was down about 123 basis points to 0.68% at the end of September. In September, the Treasury yield curve was little changed on a month-over-month basis, following moderate curve steepening in August. We believe a wave of new Treasury issuance in August put increased upward pressure on longer-term rates.

# Employment



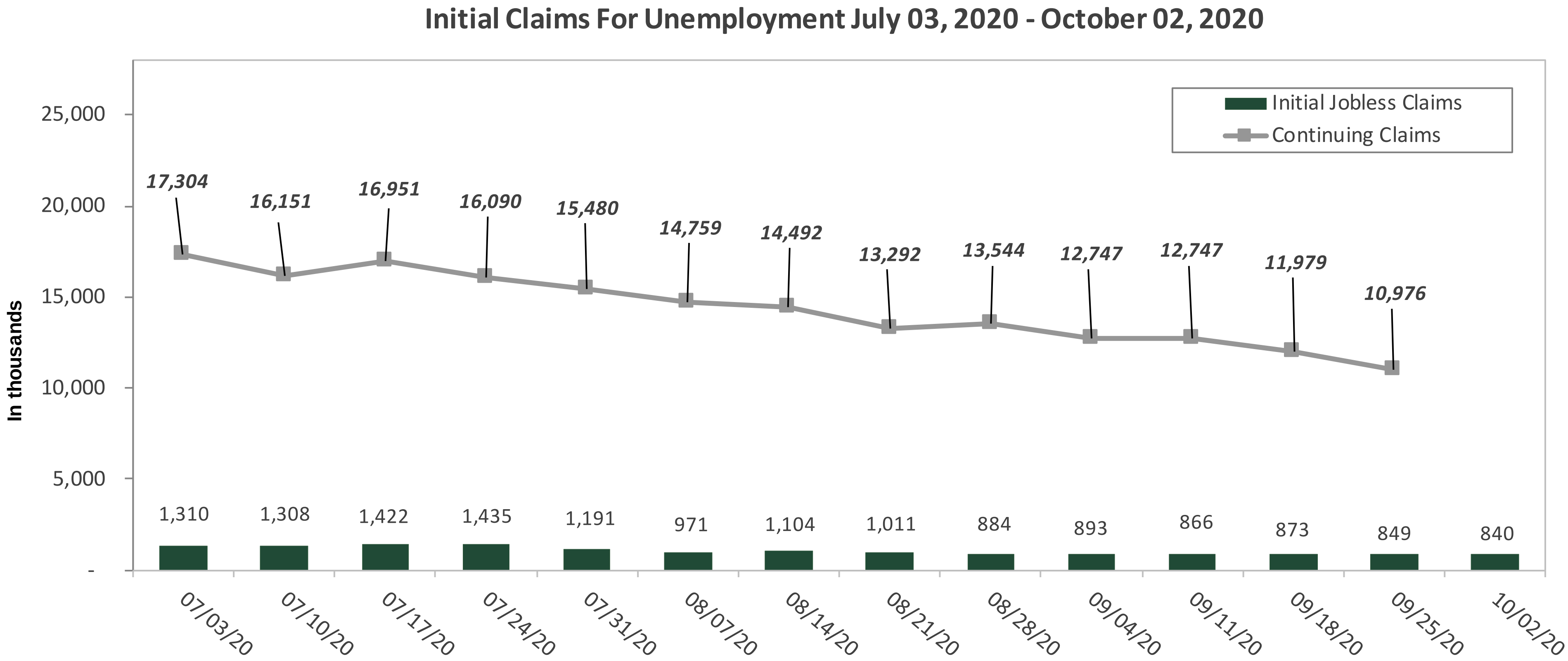

*Source: US Department of Labor*




*Source: US Department of Labor*

U.S. nonfarm payrolls were lower than expected, up 661,000 in September versus expectations of 859,000. The unemployment rate declined to 7.9% in September from 8.4% in August. The decline in the unemployment rate was better than expected, however, it was partially driven by a decline in the labor participation rate to 61.4% in September from 61.7% in August. The labor participation rate improved modestly after plunging to 60.2% in April, but remains near the lowest levels since the 1970's. Nearly 4.5 million people have dropped out of the labor force since January, and 12.6 million people in the labor force were unemployed in September, according to the U.S. Bureau of Labor Statistics household survey. Workers who classified themselves as employed but absent from work in the September survey understated the unemployment rate by about 0.4%. The U-6 underemployment rate, which includes those who are marginally attached to the labor force and employed part time for economic reasons, remained high but eased to 12.8% in September from 14.2% in August.

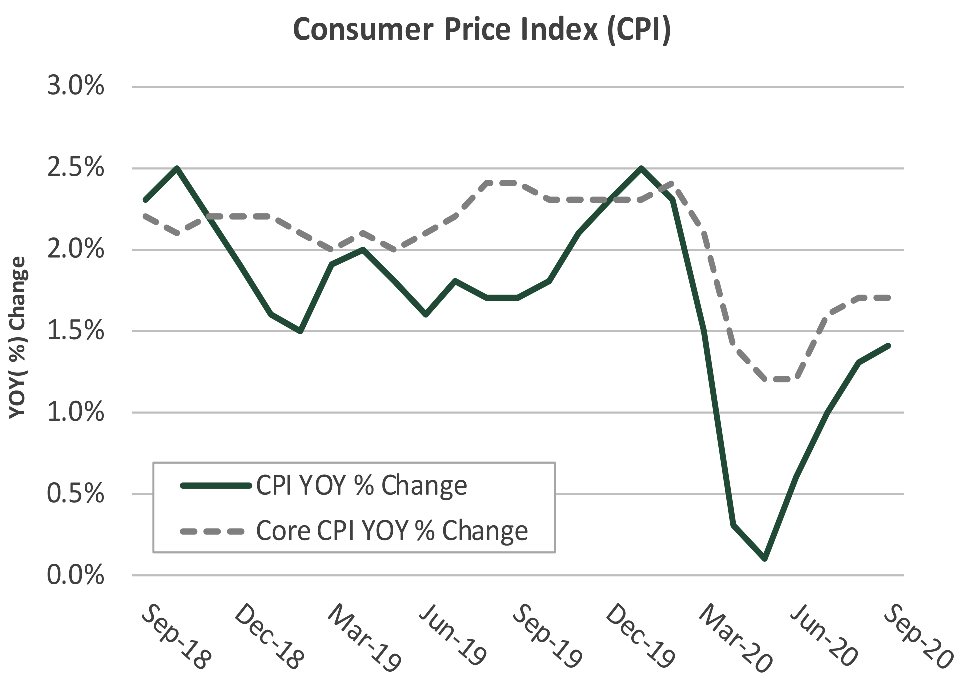
# Initial Claims for Unemployment



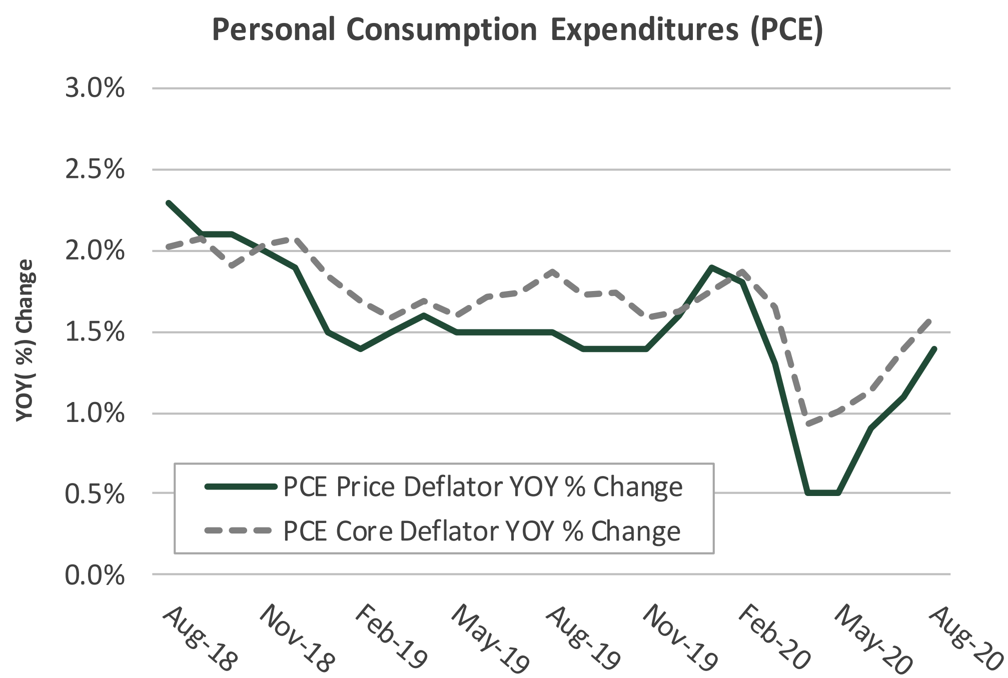

*Source: US Department of Labor*

In the most recent week, the number of initial jobless claims declined to 840,000 compared to 849,000 in the prior week. The level of continuing unemployment claims (where the data is lagged by one week) declined to about 11.0 million from roughly 12.0 million in the prior week. Continuing jobless claims have declined from the peak of nearly 25 million in early May, but they remain well above the 2019 average of 1.7 million.

# Inflation



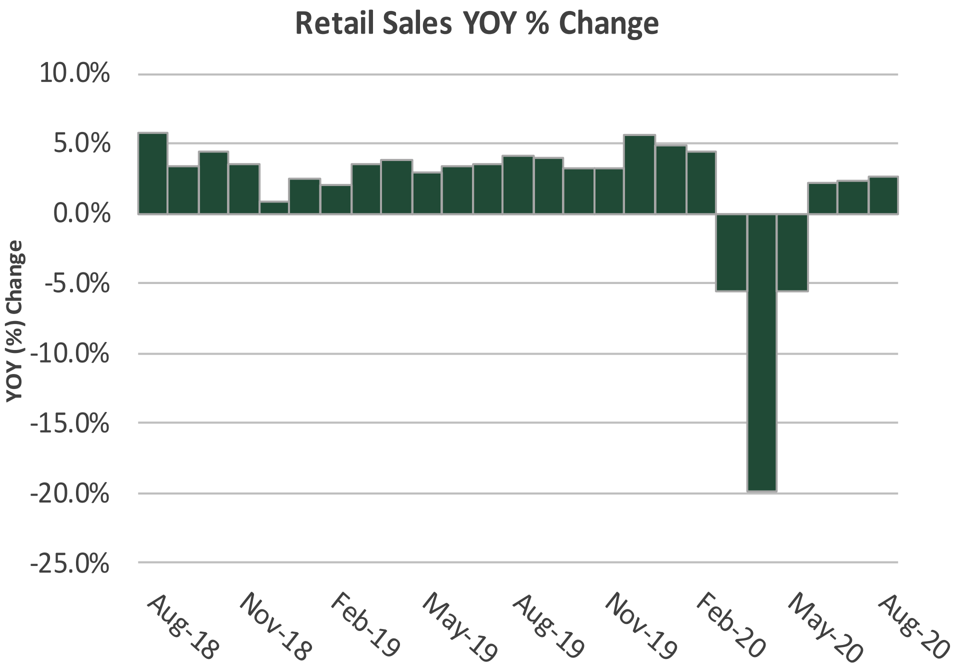

*Source: US Department of Labor*




*Source: US Department of Commerce*

The Consumer Price Index (CPI) was up 1.4% year-over-year in September, versus up 1.3% in August. Core CPI (CPI less food and energy) was up 1.7% year-over-year in September, unchanged from August. The Personal Consumption Expenditures (PCE) index was up 1.4% year-over-year in August, versus up 1.1% year-over-year in July. Core PCE, which is the Fed's primary inflation gauge, was up 1.6% year-over-year in August, versus up 1.4% year-over-year in July. Pricing pressures are increasing but remain below the Fed's inflation target.

# Consumer

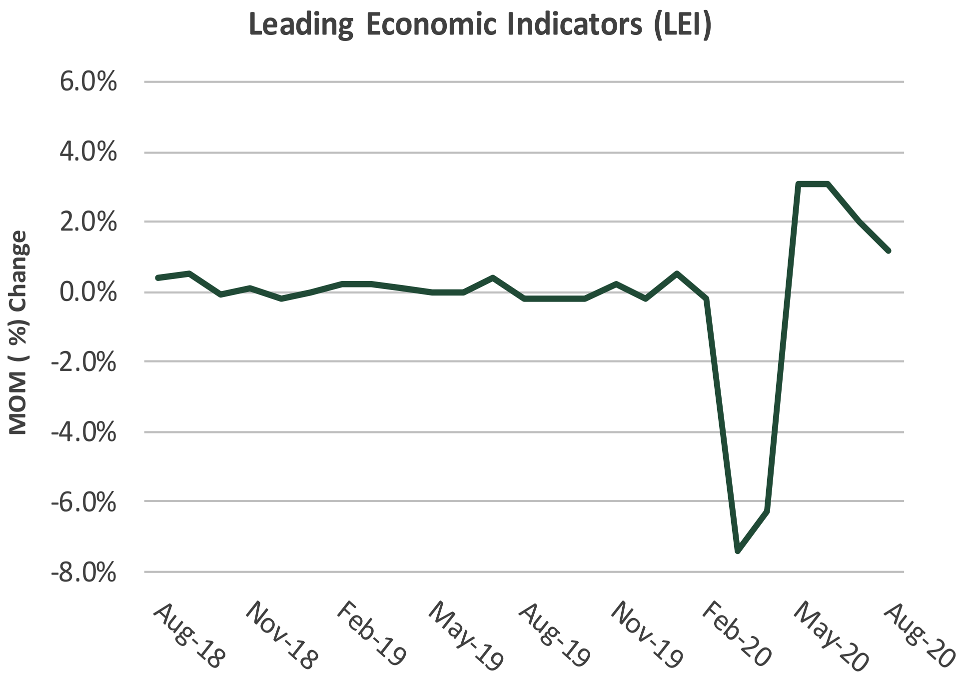



*Source: US Department of Commerce*

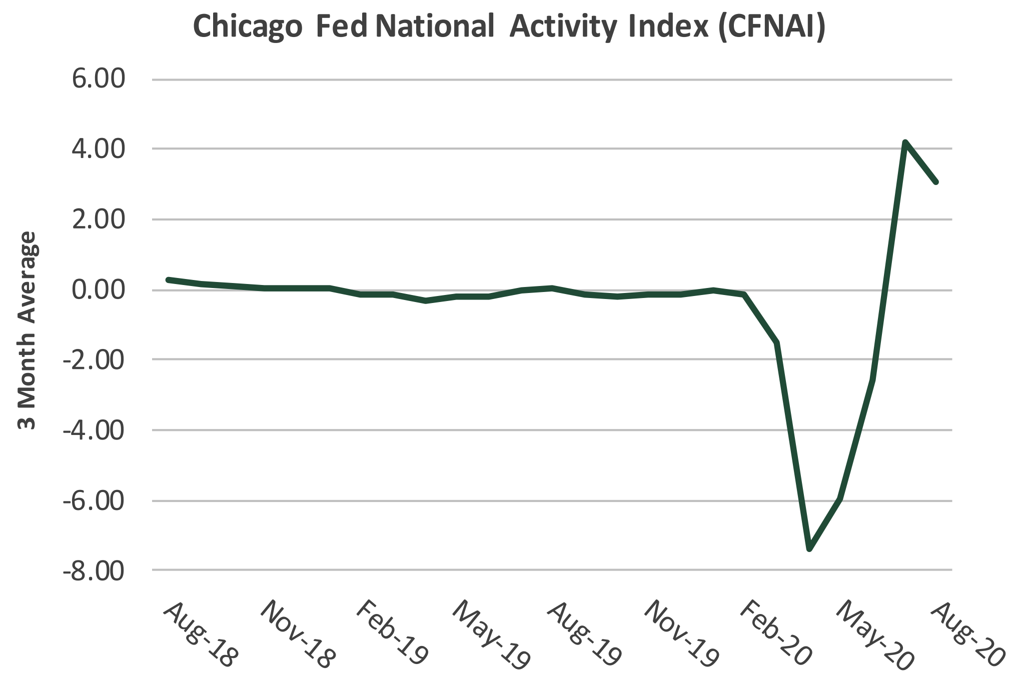

*Source: The Conference Board*

Retail sales were softer than expected in August and sales for July were revised down. On a year-over-year basis, retail sales were up 2.6% in August, versus up 2.4% in July. On a month-over-month basis, retail sales were up just 0.6% in August, following a 0.9% increase in July. Control group retail sales fell 0.2% in August, well below expectations for a 0.5% increase. The Consumer Confidence index jumped to 101.8 in September from 86.3 in August. The improvement in consumer confidence was much better than expected in September but the index remains well below pre-pandemic levels at the start of this year.

# Economic Activity



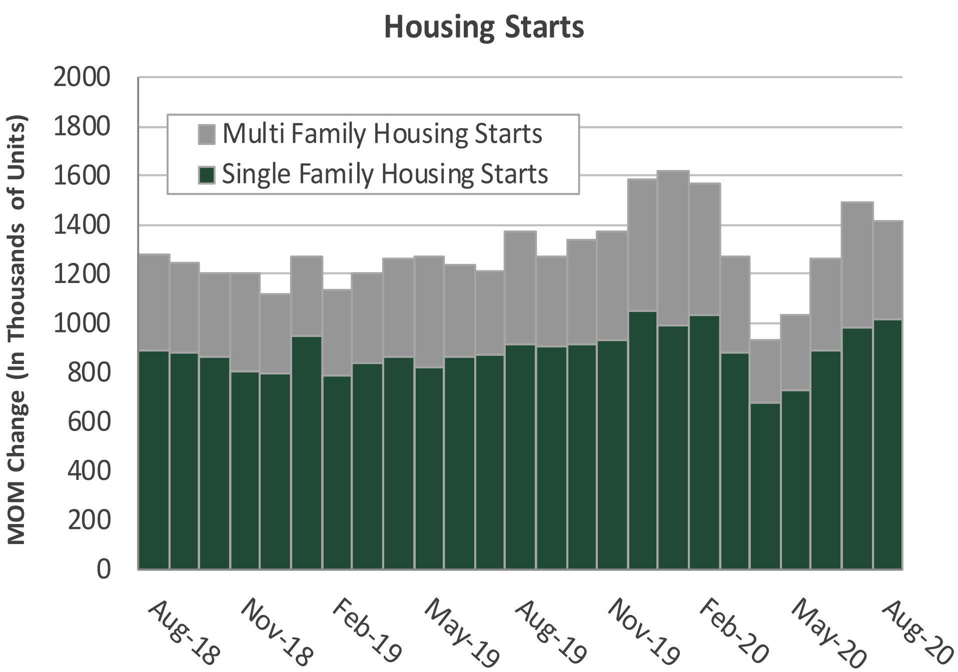

*Source: The Conference Board*



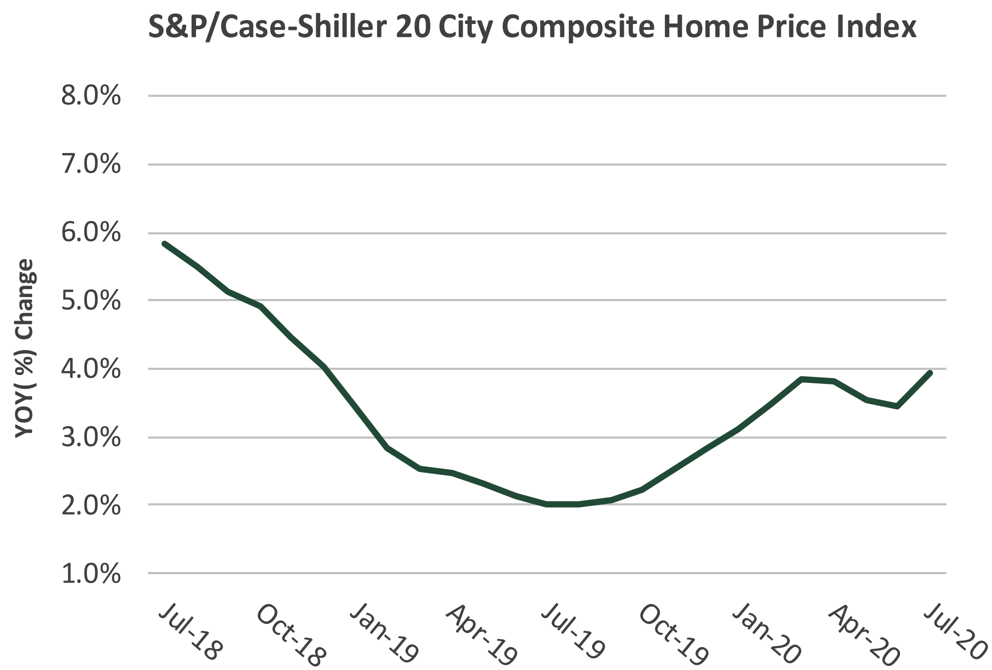

*Source: Federal Reserve Bank of Chicago*

The Conference Board's Leading Economic Index (LEI) rose 1.2% in August, following a 2.0% increase in July. On a year-over-year basis, the LEI was down 4.7% in August versus down 6.1% in July. According to the Conference Board, the recovery is losing steam and the US economy will likely head into 2021 under substantially weakened economic conditions. The Chicago Fed National Activity Index (CFNAI) declined to 0.79 in August from 2.54 in July. On a 3-month moving average basis, the CFNAI declined to 3.05 in August from 4.23 in July. Although the CFNAI declined in August on a 3-month moving basis, it is above the -0.7 recessionary level.

# Housing



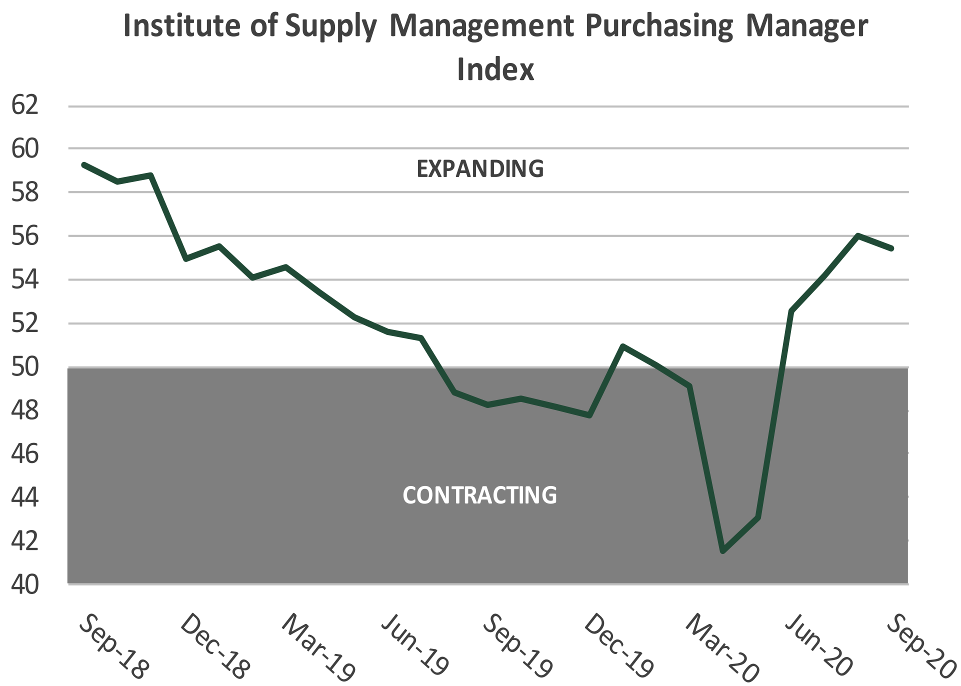

*Source: US Department of Commerce*




*Source: S&P*

Total housing starts fell 5.1% in August to an annual pace of 1,416,000. Single family starts rose 4.1% to an annualized rate of 1,021,000, while multi-family starts declined 22.7% to an annualized rate of 395,000. On a year-over-year basis, total housing starts were up 2.8% in August. Meanwhile, permits declined 0.9% in August on a month-over-month basis, to an annualized rate of 1,470,000 (flat on a year-over-year basis). According to the Case-Shiller 20-City home price index, home prices were up 3.9% year-over-year in July versus up 3.5% year-over-year in June. The housing market has remained strong during the pandemic. Very low mortgage rates, solid stock market performance, and a meaningful shift toward working from home are providing strong tailwinds for the housing sector, despite an otherwise challenging economic backdrop.

# Manufacturing




*Source: Institute for Supply Management*

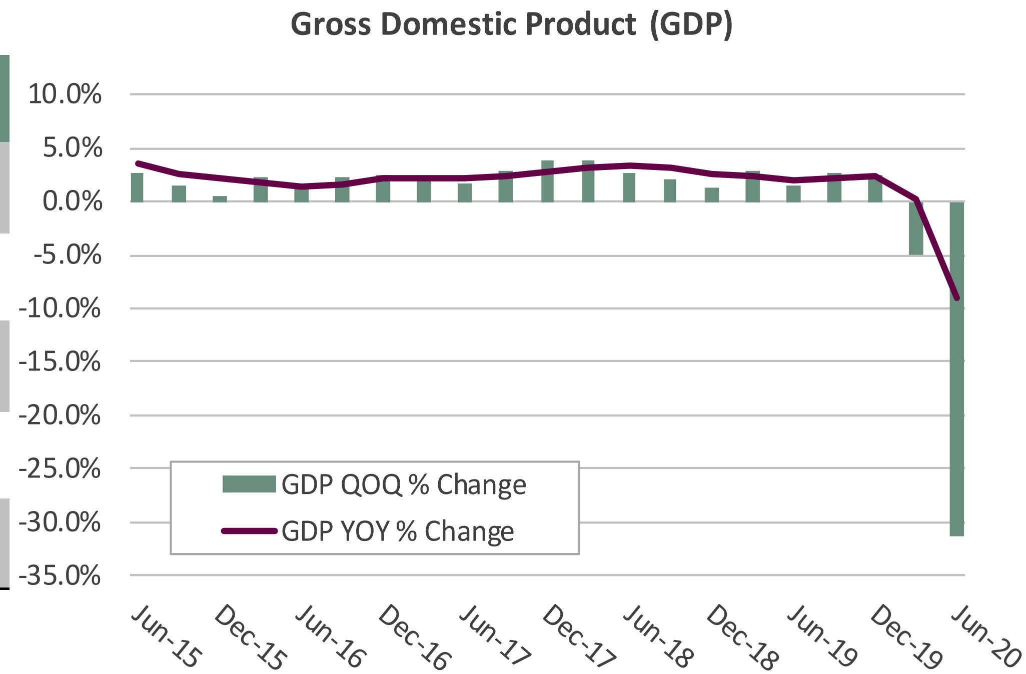

*Source: Federal Reserve*

The Institute for Supply Management (ISM) manufacturing index slipped to 55.4 in September from 56.0 in August. New orders remained strong but declined to 60.2 in September from 67.6 in August. Readings above 50.0 are indicative of expansion in the manufacturing sector. The Industrial Production index was down 7.7% year-over-year in August, versus down 7.4% in July. On a month-over-month basis, the Industrial Production index increased just 0.4% in August, missing expectations of 1.2%, following a 3.5% increase in July. Capacity Utilization improved to 71.4% in August from 71.1% in July, but remains well below the long-run average of 79.8%. Overall manufacturing conditions have improved, following a deep contraction, but the pace of improvement is slowing.

# Gross Domestic Product (GDP)

| Components of GDP | 9/19 | 12/19 | 3/20 | 6/20 |
|---|---|---|---|---|
| Personal Consumption Expenditures | 1.8% | 1.1% | -4.8% | -24.0% |
| Gross Private Domestic Investment | 0.3% | -0.6% | -1.6% | -8.8% |
| Net Exports and Imports | 0.0% | 1.5% | 1.1% | 0.6% |
| Federal Government Expenditures | 0.3% | 0.3% | 0.1% | 1.2% |
| State and Local (Consumption and Gross Investment) | 0.1% | 0.2% | 0.1% | -0.4% |
| **Total** | **2.6%** | **2.4%** | **-5.0%** | **-31.4%** |

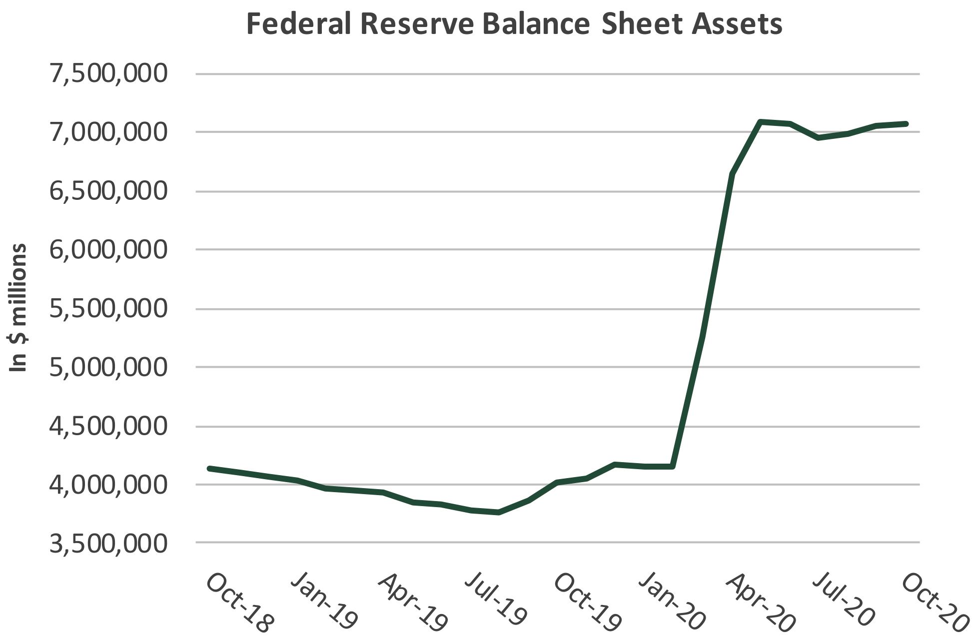
*Source: US Department of Commerce*



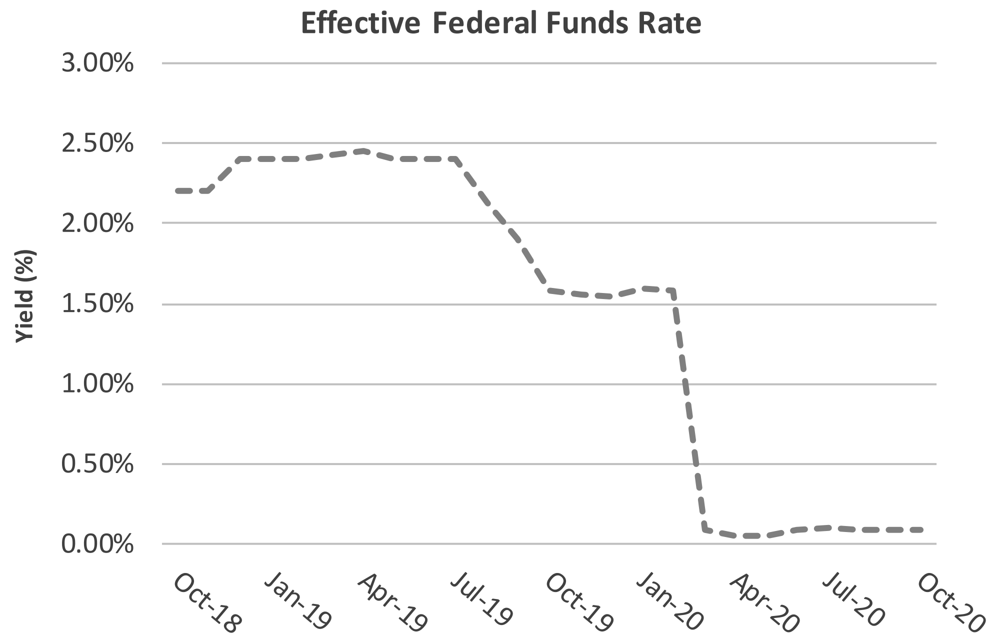

*Source: US Department of Commerce*

According to the third estimate, US gross domestic product (GDP) declined at an annual rate of 31.4% in the second quarter, just slightly less negative than the initial and second estimates but still the largest decline on record. This follows a 5.0% annualized decline in first quarter GDP. Personal consumption expenditures plunged 33.2% in the second quarter, following a 6.9% decline in the first quarter. The consensus forecast calls for a strong rebound in consumer spending and overall economic activity in the third quarter, and a slower pace of improvement in activity thereafter.

# Federal Reserve



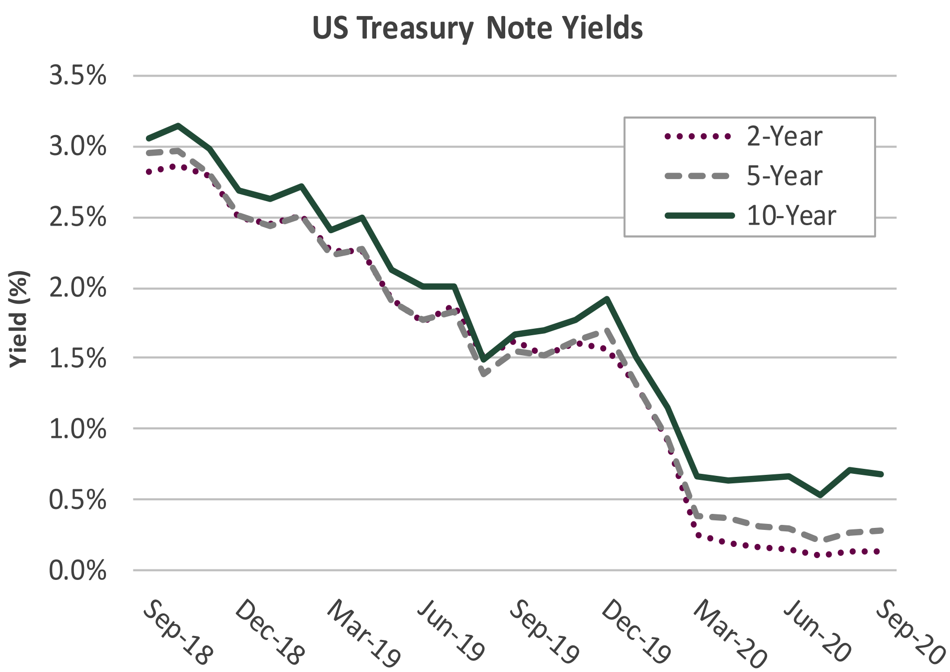

*Source: Federal Reserve*



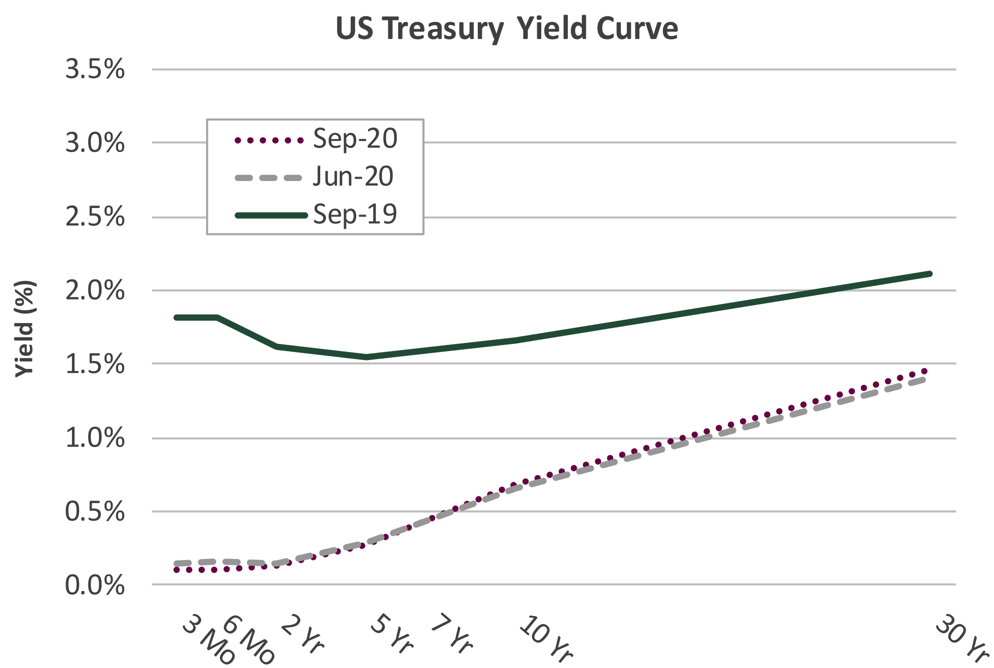

*Source: Bloomberg*

The Fed has taken a wide range of aggressive actions to help stabilize and provide liquidity to the financial markets. The Fed has lowered the fed funds target rate to a range of 0.0%-0.25% and continues to purchase Treasury and agency mortgage-backed securities to support smooth market functioning. Policymakers reinstated the Commercial Paper Funding Facility and Money Market Mutual Fund Liquidity Facility in order to provide liquidity to the commercial paper, money markets, and the municipal bond markets. The Fed has established the Primary Market Corporate Credit Facility and Secondary Market Corporate Credit Facility to support the corporate bond market. The Term Asset-Backed Securities Loan Facility has been established to enable the issuance of asset-backed securities backed by student loans, auto loans, credit card loans, and loans guaranteed by the Small Business Administration. The Fed has established the Paycheck Protection Program Liquidity Facility and Fed's Main Street Lending Facility to support the flow of credit to businesses. The Fed established the Municipal Liquidity Facility to purchase short-term debt directly from US states, counties, and cities. The Fed has also provided short-term funding through large-scale repo operations and lowered the reserve requirement for depository institutions.

# Bond Yields

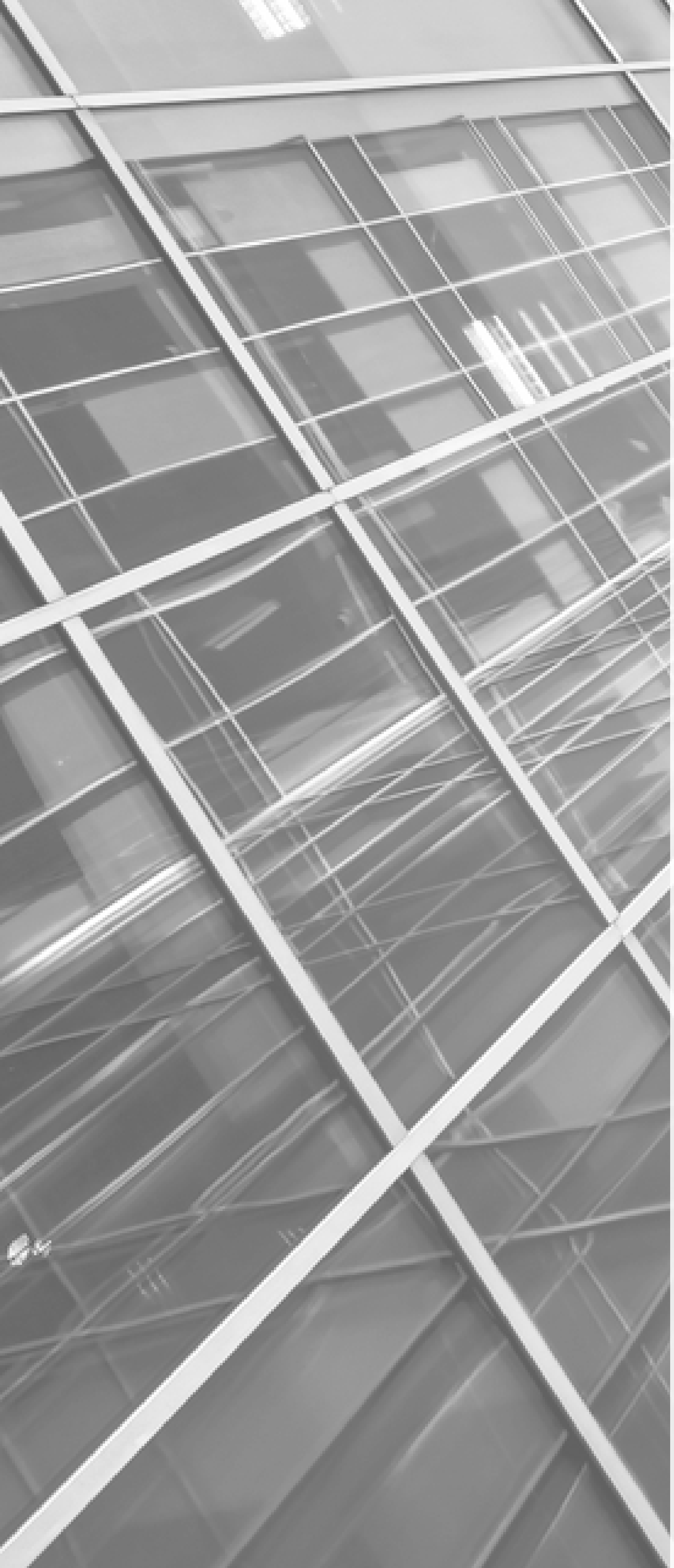



*Source: Bloomberg*




*Source: Bloomberg*

At September month-end, Treasury yields were much lower on a year-over-year basis. The 3-month T-bill yield was down 172 basis points, the 2-year Treasury yield was down 150 basis points, and the 10-Year Treasury yield was down 98 basis points, year-over-year. Yields declined precipitously in March 2020, with the Fed cutting rates by a total of 150 basis points and a flight to safe-haven assets driving down yields across the curve. The Fed has signaled plans to keep the front end of the Treasury yield curve anchored near zero for at least the next few years.



# Section 2 | Account Profile

## Investment Objectives

The Orange County Transportation Authority's investment objectives, in order of priority, are to provide safety to ensure the preservation of capital in the overall portfolio, provide sufficient liquidity for cash needs and a market rate of return consistent with the investment program.

## Chandler Asset Management Performance Objective

The performance objective for the portfolio is to earn a total rate of return through a market cycle that is equal to or above the return on the benchmark index.

## Strategy

In order to achieve these objectives, the portfolio invests in high quality fixed income securities consistent with the investment policy and California Government Code.

# Compliance

*As of September 30, 2020*

**Orange County Transportation Authority**

*Assets managed by Chandler Asset Management are in full compliance with state law and the Client's investment policy.*

| Category | Standard | Comment |
|---|---|---|
| Treasury Issues | U.S. Treasury notes, bonds, bills, or certificates of indebtedness, or those for which the faith and credit of the U.S. are pledged for the payment of principal and interest. | *Complies* |
| Federal Agencies or U.S. Government Sponsored Enterprises | Federal agency or U.S. government -sponsored enterprise obligations, participations, or other instruments, including those issued or fully guaranteed as to principal and interest by federal agencies or U.S. government -sponsored enterprises. | *Complies* |
| Supranationals | "AA" rating category or higher by a NRSRO; 20% maximum; 10% max per issuer; USD denominated senior unsecured unsubordinated obligations; Issued or unconditionally guaranteed by International Bank for Reconstruction (IBRD), International Finance Corporation (IFC), or Inter-American Development Bank (IADB) | *Complies* |
| Municipal Debt | "A" rating category or "A-1" rated or higher by a NRSRO ; 30% maximum; 5% max per issuer; Instruments Issued by local and state agency, including:<br>a) Registered state warrants, treasury notes or bonds of the State of California, including bonds payable solely out of revenues from a revenue-producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the state.<br>b) Bonds, notes, warrants, or other evidences of indebtedness of a local agency within the State of California, including bonds payable solely out of revenues from a revenue-producing property owned, controlled, or operated by the state or local agency by a department, board, agency or authority of the local agency.<br>c) Registered treasury notes or bonds of any of the other 49 states in addition to California, including bonds payable solely out of revenues from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states.<br>d) Defeased state and local obligations as long as the obligations have been legally defeased with State and Local Government Series (SLGS), U.S. Treasury, and U.S. Agency securities and such obligations mature or otherwise terminate within five years of the date of purchase. | *Complies* |
| OCTA Notes and Bonds | 25% maximum; Notes and bonds issued by OCTA, including notes and bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by OCTA or by a department, board, agency or authority of OCTA which may bear interest at a fixed or floating rate. | *Complies* |
| Banker's Acceptances | "A-1" rated or higher by 2 NRSROs; 30% maximum; 5% max per issuer; 180 days max maturity | *Complies* |
| Commercial Paper | "A-1" rated or higher by 2 NRSROs; Issued by corporations that have debt other than commercial paper, if any, that is rated A-1 or higher by a NSRSRO; 25% maximum; 270 days max maturity; Issued by corporation organized and operating within the U.S. with assets >$500 million; 10% max of the outstanding paper of the issuing corporation. | *Complies* |
| Negotiable Certificates of Deposit (NCD) | "A" rating category or "A-1" rated or higher by 2 NRSROs; 30% maximum; 5% max per issuer; Issued by nationally or state-chartered bank or state, a savings association or a federal association, a state or federally licensed or state licensed branch of a foreign bank. | *Complies* |
| Corporate Medium Term Notes | "A" rating category or better by a NRSRO; 30% maximum; 5% max per issuer; Corporate and depository institution debt securities issued by corporations organized and operating within the U.S. or by depository institutions licensed by the U.S. or any state and operating within the U.S. | *Complies* |
| Mortgage and Asset-backed Securities | "AA" rating category or higher by a NRSRO; 20% maximum (combined); 10% maximum on ABS; 5% max per issuer; Any mortgage pass-through security, collateralized mortgage obligation, mortgage-backed or other pay-through bond, equipment lease-backed certificate, consumer receivable pass-through certificate, or consumer receivable-backed bond. | *Complies* |
| Money Market / Mutual Funds | "AAA" rated or equivalent by 2 NRSROs; 20% maximum; 10% max of the fund's or pool's asset; 10% max per Money Market Mutual Fund; 10% max per Mutual Fund. | *Complies* |
| Local Agency Investment Fund (LAIF) | $75 million per account; Pooled fund managed by the State Treasurer; Not used by Investment Adviser | *Complies* |
| Orange County Treasury Investment Pool (OCIP) | 10% maximum; Pooled fund managed by the Orange County Treasurer; Comprised of two funds: the Money Market Fund and Extended Fund | *Complies* |
| Joint Powers Authority (JPA) Investment Pools | 10% maximum; Shares of beneficial interest issued by a joint powers authority pursuant to California Government Code | *Complies* |
| Variable and Floating Rate Securities | 30% maximum; Must utilize traditional money market reset indices such as US Treasury bills, Federal Funds, commercial paper or LIBOR, or SOFR, and meet credit requirements detailed in Investment Policy; Investments in floating rate securities whose reset is calculated using more than one of the above indices are not permitted, (i.e. dual index notes) | *Complies* |
| Bank Deposits | A-1 short-term rating or equivalent or higher by a NRSRO; 5% maximum; Collateralized as specified under Government Code section 53630 | *Complies* |
| Repurchase Agreements | "A" rating category or "A-1" rated or higher by 2 NRSROs; 25% maximum; Collateralized by U.S. Treasuries or Agency securities; Not used by Investment Adviser. | *Complies* |
| Derivatives | Must be approved by the Finance and Administration Committee prior to entering into such investment; Not used by Investment Adviser | *Complies* |
| Prohibited | Inverse floaters, Range notes, Strips derived from mortgage obligations, Step-up notes, Dual index notes; Investments returning a zero or negative yield if held to maturity; Reverse Repurchase Agreements only permitted within a JPA investment pool. | *Complies* |
| Negative Credit Watch/<br><br>Credit Rating Actions | If an eligible security already contained in the Authority's portfolio is subsequently placed on "Negative Credit Watch" (Credit Watch) by any of the 3 NRSROs, then the security will be handled under the provisions of Credit Rating Actions; Percentage holding limits and credit quality minimums are applicable at the time of purchase.<br><br>Credit Rating Actions: Rating criteria will apply at the time of purchase of a security and monitored for changes while retained within OCTA's portfolio. A security whose credit rating has been placed on Credit Watch, or whose credit rating has been downgraded (including downgrades resulting in the rating falling below the minimum credit rating requirements subsequent to the time of purchase, is not a violation of OCTA's Investment Policy. Investment Managers are to notify OCTA regarding any security whose credit rating has been placed on Credit Watch or downgraded. The notice shall include a risk assessment based on OCTA's Investment Objectives, and a recommendation to retain or sell the security. The security shall be immediately reviewed by the Treasurer for action. The decision to retain the security, sell the security, or other action shall be approved by the Treasurer. | *Complies* |
| Max Per Issuer/ Counter-Party | 5% max per issuer/counterparty for all securities except U.S. Treasuries and U.S. Government Agency Securities; Unless otherwise specified in the policy, any one corporation, bank, local agency, special purpose vehicle or other corporate issuer name for one or more series of securities shall not exceed 5% of the portfolio. | *Complies* |
| Maximum maturity | 5 years | *Complies* |

# Portfolio Characteristics

*As of September 30, 2020*

**Orange County Transportation Authority**

| | 9/30/2020 | | 6/30/2020 |
|---|---|---|---|
| | Benchmark* | Portfolio | Portfolio |
| **Average Maturity (yrs)** | 1.87 | 1.94 | 1.99 |
| **Average Modified Duration** | 1.83 | 1.84 | 1.86 |
| **Average Purchase Yield** | n/a | 1.75% | 1.92% |
| **Average Market Yield** | 0.13% | 0.23% | 0.30% |
| **Average Quality**** | AAA | AA+/Aa1 | AA+/Aa1 |
| **Total Market Value** | | 411,140,897 | 410,306,892 |

**ICE BAML 1-3 Yr US Treasury Index*

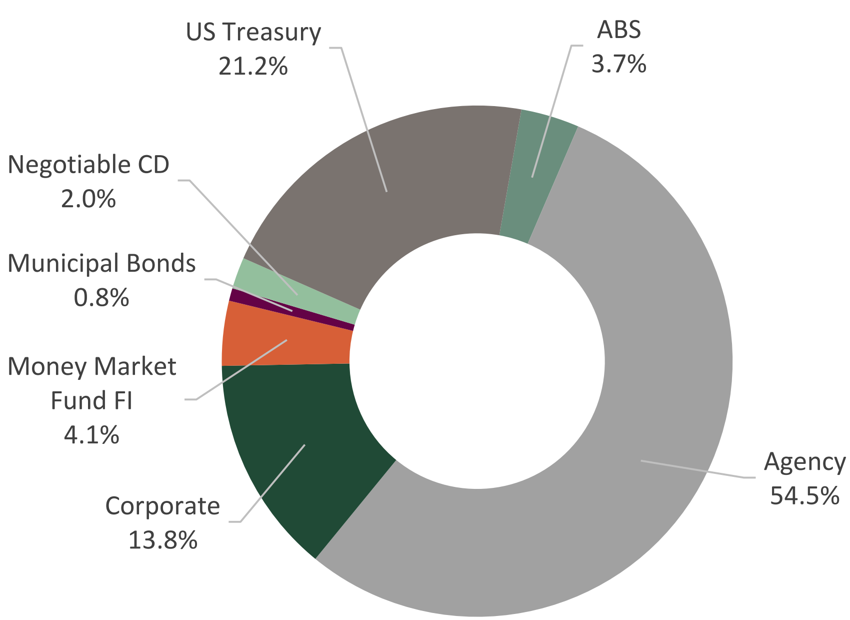
***Benchmark is a blended rating of S&P, Moody's, and Fitch. Portfolio is S&P and Moody's respectively.*

# Sector Distribution

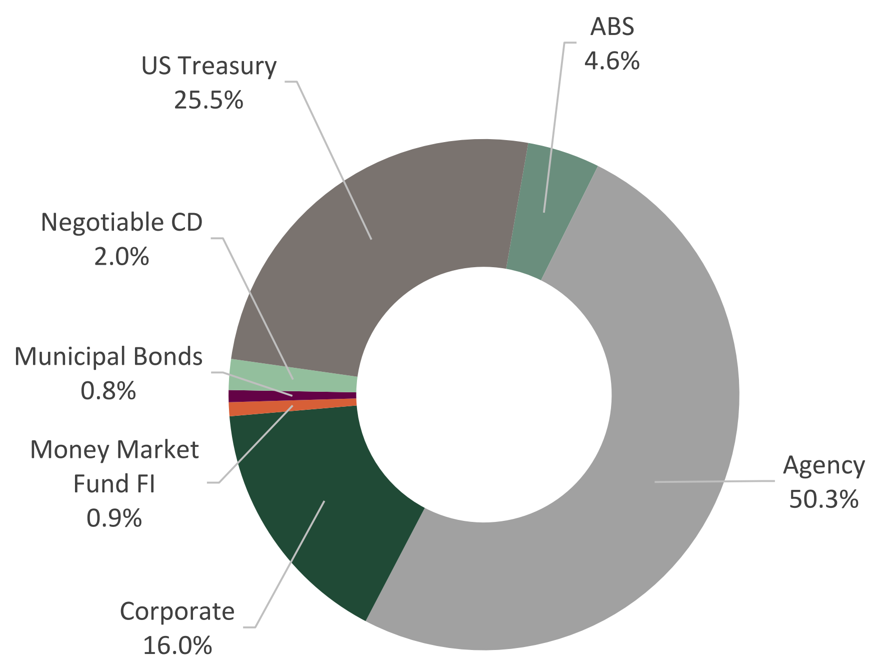
*As of September 30, 2020*

**Orange County Transportation Authority**

**September 30, 2020**




**June 30, 2020**



# Issuers

*As of September 30, 2020*

## Orange County Transportation Authority – Account #10587

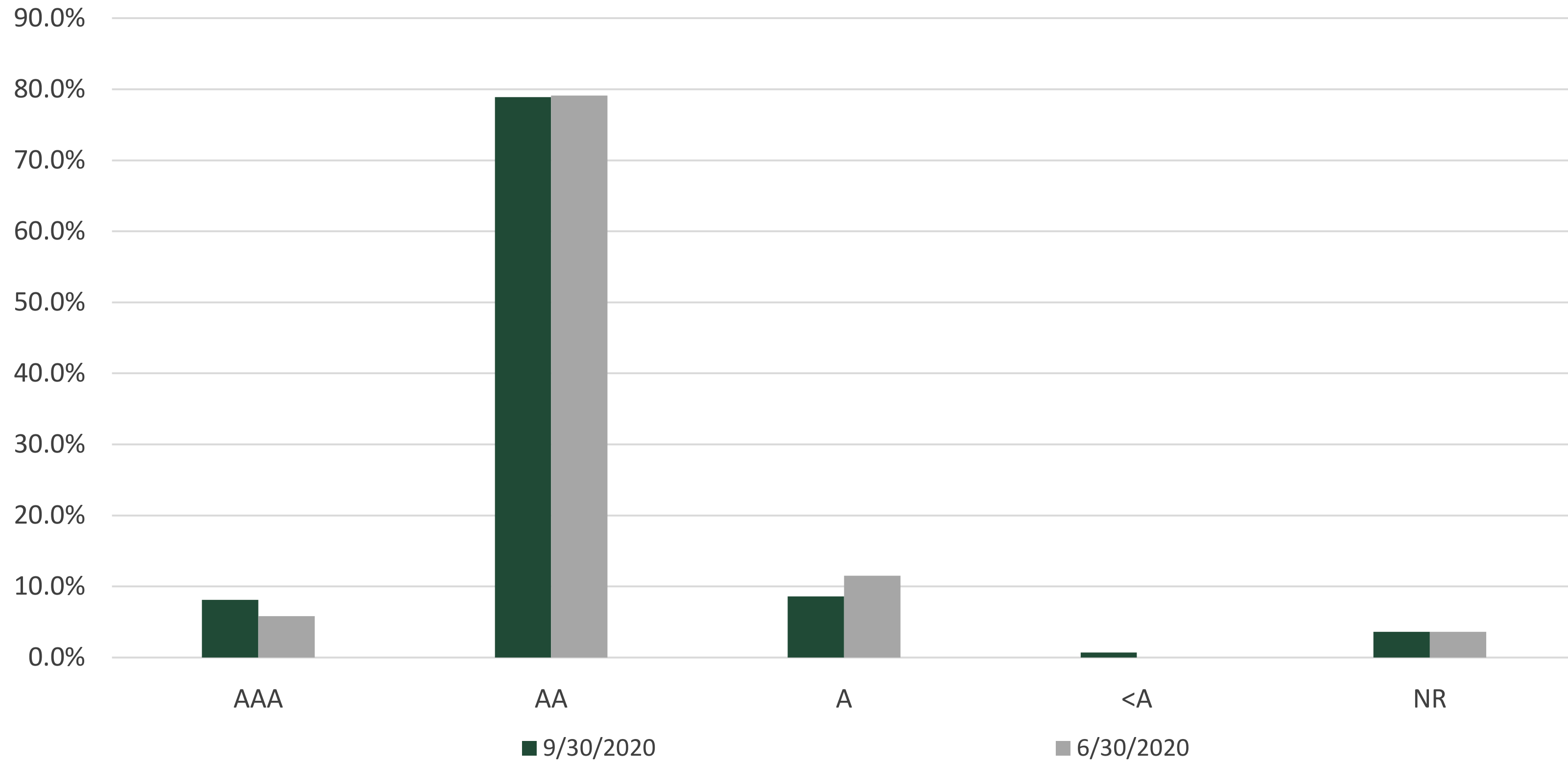
| Issue Name | Investment Type | % Portfolio |
|---|---|---|
| Government of United States | US Treasury | 21.22% |
| Federal Farm Credit Bank | Agency | 17.59% |
| Federal Home Loan Bank | Agency | 14.50% |
| Federal Home Loan Mortgage Corp | Agency | 12.80% |
| Federal National Mortgage Association | Agency | 9.61% |
| First American Govt Obligation Fund Class-Z | Money Market Fund FI | 4.12% |
| Royal Bank of Canada | Negotiable CD | 1.95% |
| Honda ABS | ABS | 1.62% |
| Wal-Mart Stores | Corporate | 1.32% |
| Apple Inc | Corporate | 1.29% |
| Berkshire Hathaway | Corporate | 1.28% |
| Oracle Corp | Corporate | 1.01% |
| General Dynamics Corp | Corporate | 1.00% |
| Paccar Financial | Corporate | 0.95% |
| Praxair | Corporate | 0.94% |
| Honda Motor Corporation | Corporate | 0.91% |
| John Deere ABS | ABS | 0.88% |
| Bank of America Corp | Corporate | 0.78% |
| Bank of New York | Corporate | 0.77% |
| State of New York | Municipal Bonds | 0.77% |
| Wells Fargo Corp | Corporate | 0.74% |
| Nissan ABS | ABS | 0.74% |
| Deere & Company | Corporate | 0.71% |
| Toyota Motor Corp | Corporate | 0.62% |
| US Bancorp | Corporate | 0.53% |
| Visa Inc | Corporate | 0.52% |
| Charles Schwab Corp/The | Corporate | 0.39% |
| Mercedes-Benz Auto Lease Trust | ABS | 0.35% |
| Toyota ABS | ABS | 0.08% |
| **TOTAL** | | **100.00%** |

# Quality Distribution

*As of September 30, 2020*

**Orange County Transportation Authority**

**September 30, 2020 vs. June 30, 2020**




| | AAA | AA | A | <A | NR |
|---|---|---|---|---|---|
| 09/30/20 | 8.1% | 78.9% | 8.6% | 0.7% | 3.6% |
| 06/30/20 | 5.8% | 79.1% | 11.5% | 0.0% | 3.6% |

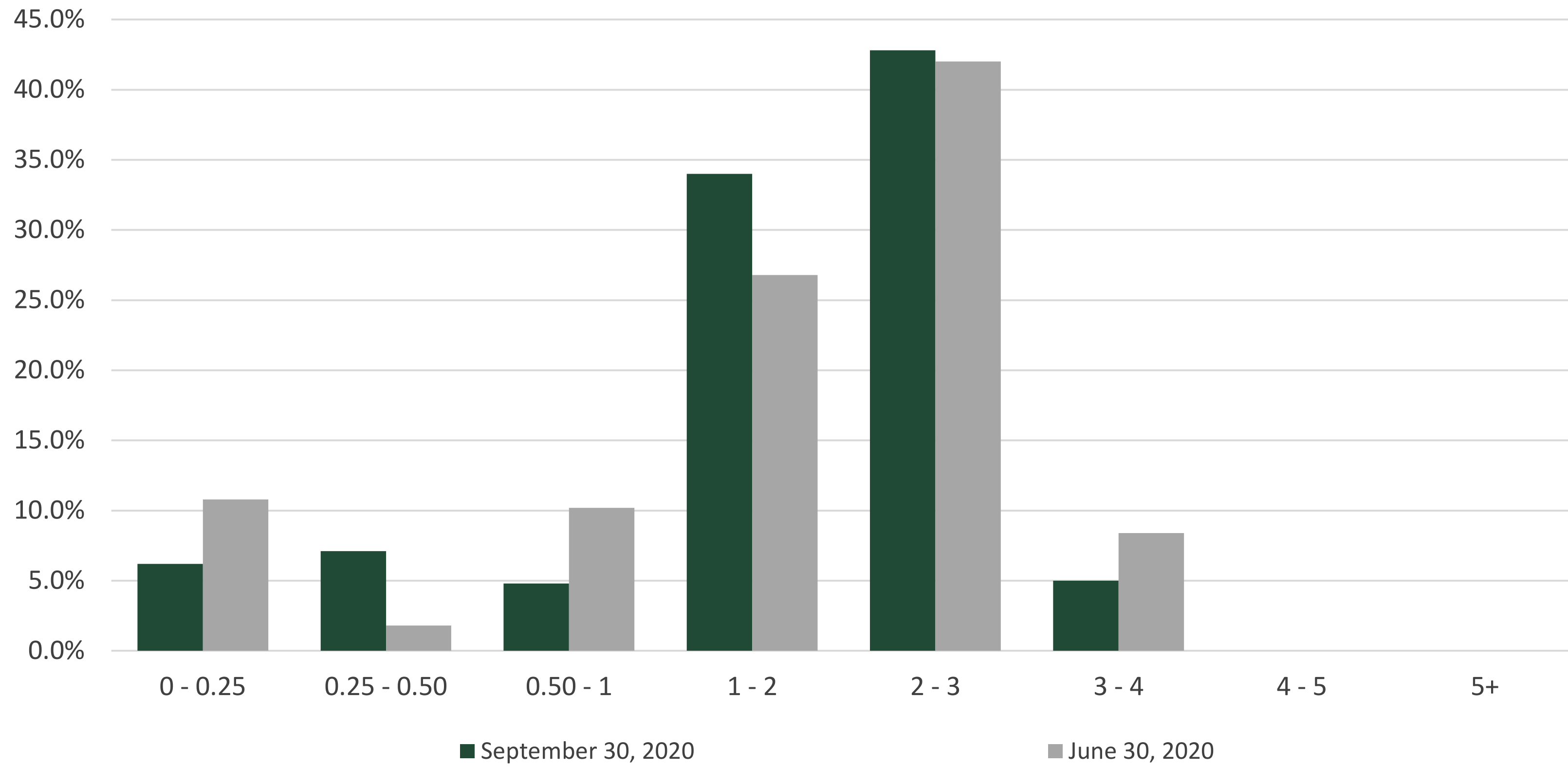
*Source: S&P Ratings*

# Duration Distribution

*As of September 30, 2020*

**Orange County Transportation Authority**

**September 30, 2020 vs. June 30, 2020**




| | 0 - 0.25 | 0.25 - 0.50 | 0.50 - 1 | 1 - 2 | 2 - 3 | 3 - 4 | 4 - 5 | 5+ |
|---|---|---|---|---|---|---|---|---|
| 09/30/20 | 6.2% | 7.1% | 4.8% | 34.0% | 42.8% | 5.0% | 0.0% | 0.0% |
| 06/30/20 | 10.8% | 1.8% | 10.2% | 26.8% | 42.0% | 8.4% | 0.0% | 0.0% |